In the Supreme Court of the United States.

OCTOBER TERM, 1964.

No. 35

SECURITIES AND EXCHANGE COMMISSION,
Petitioner,

v.

AMERICAN TRAILER RENTALS COMPANY,
Respondent.

AMICUS CURIAE BRIEF OF STATE MUTUAL LIFE ASSURANCE COMPANY OF AMERICA, THE GEORGE PUTNAM FUND OF BOSTON AND THE PUTNAM MANAGEMENT COMPANY, INC.

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AMICUS CURIAE BRIEF OF STATE MUTUAL LIFE ASSURANCE COMPANY OF AMERICA, THE GEORGE PUTNAM FUND OF BOSTON AND THE PUTNAM MANAGEMENT COMPANY, INC., Appellees in *S.E.C.* v. *Burton* (1st Cir. No. 6623 Pending) involving American Guaranty Corporation* and owners of senior and subordinated debt and stocks of that debtor constituting about one-eighth of its total capital.

Question Presented Here.

Is a District Court's denial of a motion by the Petitioner Commission under Section 328 of the Bankruptcy Act to

* The official Committee of Creditors of American Guaranty Corporation, the Debtor itself and its Receiver concur in the position argued in this brief. See the separate statement of the Committee of Creditors on page 22, *infra*.

transfer a reorganization proceeding from Chapter XI to Chapter X an abuse of that Court's discretion where the accepted plan of arrangement for a hopelessly bankrupt corporation turns creditor claims, including those of public investors, into shares of a new corporation organized to take over the debtor's business in which the debtor's stockholders receive for their equity interest about 12% of those shares, restricted in voting, dividend and liquidation rights?

Statement of Facts and Proceedings Below.

American Trailer Rentals Company ("American"), formed in 1958 to operate as part of a trailer rentals system and later growing through mergers in 1961 to become the whole of that system, is the debtor in this case. The trailers in the system, which attached to the rear of automobiles, were rented to the general public by service station operators located throughout the country.

The trailers were originally sold by the debtor to individuals, many of whom were public investors, who then leased them back to the debtor under one of the three following arrangements (R. 3, 152):

(1) 2% of cost per month for 10 years

(2) 3% of cost per month for 5 years

(3) 35% of net rental income

Most of the owners chose either (1) or (2), and these choices, unrelated as they were to actual income, led to the debtor's bankruptcy when the system failed to generate sufficient revenue.

The debtor filed a petition under Chapter XI of the Bankruptcy Act on December 20, 1962. An amended plan of arrangement (R. 4, 149) has been worked out under the terms of that Chapter whereby a new company, Capitol Leasing Corporation ("Capitol"), was formed to carry on the debtor's business.

Under the plan the stock of Capitol is to be distributed to the trailer owners (who will assign their trailers to the new company), unsecured creditors and the stockholders of American in the following manner:

1. Trailer Owners and those who paid for trailers never manufactured (see Footnote 5 of the Opinion in the Court of Appeals, 325 F. 2d 47, 49 (10th Cir. 1963) (R. 154))—one share for each $2 of their remaining investment, all payments under the lease-back agreements to be treated as a return of capital and the trailer owners to waive all claims for money due or to become due under the lease-back agreements (R. 5, 154)[1].

2. Unsecured Creditors—one share of Capitol for each $3.50 of debt owed by American, except if a creditor was part of the "management" of American, then one share of Capitol for each $5.50 of debt (R. 6, 148).

3. Shareholders—107,100 shares for the assignment of the rental network consisting of arrangements with about 500 service station operators throughout the country to keep trailers on their property and rent them to the public (R. 5, 154).

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[1] Trailer owners are of course free to keep these trailers and not take part in the Plan. Of the 3,000 trailers involved at the date of the petition (R. 153), about 700 had been so withdrawn and 299 had been exchanged for shares as per item 1 above.

Thus, Capitol's securities are to be issued as follows:

	Claims	*Shares in Capitol*	*Ownership in Capitol*
1. Trailer Owners			
A. Those expected to exchange approximately 2,000 trailers for shares under Plan ..	$1,021,932	510,966	58.0%
B. Those ordering trailers never manufactured	200,766	100,388	11.4
C. Shares of Capitol outstanding, all of which were issued for assignment of 299 trailers (R. 5)	176,665	88,332	10.0
			79.4%
2. Unsecured Creditors			
A. Creditors who are not management	76,394.50	21,827	2.5
B. Creditors who are management	288,238.50	52,407[2]	6.0
3. Shareholders—for rental network carried as intangible asset at $500,000 (R. 153)		107,100[2]	12.1
		881,020	100.0%

The Securities and Exchange Commission, acting pursuant to Section 328 of the Bankruptcy Act (11 U.S.C. §728) moved in the United States District Court for the District of Colorado to dismiss the proceedings under Chapter XI unless the debtor amended its petition to comply with Chapter X (R. 8). The District Court, after suggesting certain modifications to the plan of arrangement (which led

[2] Five-year suspension on voting rights, dividends and rights in liquidation (R. 148).

to the provision that creditors who were identified with the management of the debtor get only one share of Capitol for each $5.50 of debt owed to them instead of the $3.50 rate for other creditors (R. 146, 148)), denied the Commission's motion (R. 144-148), and confirmed the amended Plan. On appeal to the Court of Appeals for the Tenth Circuit, the ruling of the District Judge was unanimously affirmed (325 F. 2d 47; R. 151-161). This Court has granted the Securities and Exchange Commission's petition for a writ of certiorari to the Tenth Circuit.

The petition and accompanying brief and the writ encompass only the propriety of the Circuit Court's action in affirming the denial of the Petitioner's motion in the District Court to transfer the proceedings to Chapter X, (page 2 of the Petition and Question presented p. 2 of Petitioner's Brief in the case). This matter was involved in appeal No. 7392 to the Circuit Court (Footnote 1, R. 152). Neither the petition nor writ in this cause undertakes a review of the other appeal to the Circuit, No. 7474 confirming the modified arrangement. (See Footnote 1, R. 152).

The Interest of the Amicus Curiae.

The position argued in this brief is that whatever result may be reached in this case now before the Court, it is not, as the Petitioner's brief contends, mandatory to make such a transfer in all cases where public investor creditor interests do not receive complete priority for their claims. This position is crucial in the case on the docket of the First Circuit Court of Appeals, No. 6223, entitled *Securities and Exchange Commission* v. *Burton* (District Court Opinion *sub nom. In re American Guaranty Corp.*, 221 F. Supp. 961 (D.R.I. 1963)), in which those filing this brief are

parties and which case was brought to this Court's attention in Footnote 5, page 16 of the Petitioner's petition for a writ of certiorari in this case at bar.

We urge that should the Court rule in favor of the Petitioner on this appeal, that it make plain its decision is not controlling in the *Burton* case where, under the plan of arrangement there presented, the creditors have complete control of the debtor until all debts are paid in full and the only priority denied public investor creditors and other creditors is at most a two-year interest moratorium on their claims, thus making the facts in that case as to the nature of and effect upon public investor creditor interests very different from those in the present case.

Statutes Involved.

Bankruptcy Act:

Chapter X, Section 130 (11 U.S.C. §530)

Every petition shall state— . . .(7) the specific facts showing the need for relief under this chapter and why adequate relief cannot be obtained under chapter 11 of this title; . . .

Chapter X, Section 147 (11 U.S.C. §547)

Amendment of Petition to Comply with Provisions Governing Arrangements

A petition filed under this chapter improperly because adequate relief can be obtained by the debtor under chapter 11 of this title may, upon the application of the debtor, be amended to comply with the requirements of chapter 11 for the filing of a debtor's petition, and shall thereafter for the purposes of chapter 11 be deemed to have been originally filed thereunder.

Chapter XI, Section 328 (11 U.S.C. §728)

Dismissal, Proceedings; Amended Petition

The judge may, upon application of the Securities and Exchange Commission or any party in interest, and upon such notice to the debtor, to the Securities and Exchange Commission, and to such other persons as the judge may direct, if he finds that the proceedings should have been brought under chapter 10 of this title, enter an order dismissing the proceedings under this chapter, unless, within such time as the judge shall fix, the petition be amended to comply with the requirement of chapter 10 of this title for the filing of a debtor's petition or a creditors' petition under such chapter, be filed. Upon the filing of such amended petition, or of such creditors' petition, and the payment of such additional fees as may be required to comply with section 532 of this title, such amended petition or creditors' petition shall thereafter, for all purposes of chapter 10 of this title, be deemed to have been originally filed under such chapter.

Chapter XI, Section 366 (11 U.S.C. §766)

Requisites for Confirmation

The court shall confirm an arrangement if satisfied that —(1) the provisions of this chapter have been complied with; (2) it is for the best interests of the creditors and is feasible; (3) the debtor has not been guilty of any of the acts or failed to perform any of the duties which would be a bar to the discharge of a bankrupt; and (4) the proposal and its acceptance are in good faith and have not been made or procured by any means, promises, or acts forbidden by this title.

Confirmation of an arrangement shall not be refused solely because the interest of a debtor, or if the debtor is a corporation, the interests of its stockholders or members will be preserved under the arrangement.

Summary of Argument.

Bankruptcy Act, Section 328, under which was made the Petitioner's motion to transfer a Chapter XI proceeding to Chapter X gives the District Judge discretion, not to be reversed unless its exercise was "beyond allowable bounds." There has been no showing that adequate relief cannot be obtained in Chapter XI for this financially distressed corporation with only unsecured debt. This Court has stated that the presence of public investor creditors does not preclude use of Chapter XI and preservation of stock interests is clearly permitted by Section 366 of the Bankruptcy Act. The deletion of the "fair and equitable" requirement for Chapter XI plans by 1952 amendments means that absolute priority of creditors over equity interests is no longer essential to a plan of arrangement. The proper statutory test is only whether the plan is "in the best interests of creditors and feasible." There is no review presented here of the rulings that the plan in this case met these requirements. The denial of the transfer motion was not "beyond allowable bounds."

In *Securities and Exchange Commission* v. *Burton* (First Circuit No. 6223 Pending), where those submitting this *amicus curiae* brief are appellees, the only denial of absolute priority for public investor creditors involves a two-year waiver of interest. An independent receiver is in possession, and public investors are as protected as they would be in a Chapter X proceeding and will receive more than in a liquidation.

Any ruling that this Court may make in favor of the Petitioner in this case at bar should not effect the question presented in the *Burton* case where the facts are substantially different from those at bar.

Argument.

I. A District Court Is Not Required to Transfer a Reorganization Case from Chapter XI to Chapter X of the Bankruptcy Act Where a Plan of Arrangement Provides Shares in a New Corporation for all Creditors, Including Public Investors, on a Scaled Down Basis Leaving Shareholders of the Debtor About 12% of the New Corporation's Shares With Restricted Voting, Dividend and Liquidation Rights.

This Court has decided in *General Stores Corp.* v. *Shlensky,* 350 U.S. 462 (1956), that the general test against which the discretionary action of a District Court hearing a Section 328 motion is to be measured is "the needs to be served" (350 U.S. at 468). The application of this "Delphic" test and principle to the facts of each case may well reach different results in different cases, and this was recognized in *General Stores, supra,* where it was pointed out that:

> [a] large company with publicly-held securities may have as much need for a simple composition of unsecured debts as a smaller company. (350 U.S. at 466)

From this language and from the opinion in *In re Grayson-Robinson Stores, Inc.,* 215 F. Supp. 921, 935 (S.D.N.Y. 1963), aff'd *sub nom. Grayson-Robinson Stores, Inc.* v. *Securities and Exchange Commission,* 320 F. 2d 940 (2d Cir. 1963), the Circuit Court in the case at bar quite properly concluded that the "mere existence of public investors does not preclude use of Chapter XI." (325 F. 2d at 50) (R. 156)

The controlling statutory word, "may" in Section 328, "surely not the strongest auxiliary verb in the language", (*Grayson-Robinson Stores, Inc.* v. *Securities and Exchange*

Commission, supra, 320 F. 2d at 948), is one giving the lower court discretion, reversible as noted above only if the action "transcended allowable bounds." (*General Stores Corp.* v. *Shlensky, supra,* 350 U.S. at 468)

The Petitioner takes the position that corporate reorganizations under Chapter XI may not scale down in any manner the creditor priority of public investors. The contention is that ● District Judge has no discretion but is required to transfer to Chapter X on a motion under Section 328 any proceeding under Chapter XI attempting to limit claims of the public and preserve the interests of the stockholders. This is in contradiction of the clear discretionary language of Section 328 and the language of Section 366 which provides:

> . . . Confirmation of an arrangement shall not be refused solely because . . . the interests of [the debtor's] stockholders or members will be preserved under the arrangement. (11 U.S.C. §766)

Four District Courts have recently held the Commission's contention fallacious and refused to order transfers.[3] The facts of each case may well warrant different results, but under the present Chapter XI there is no absolute requirement that a transfer be ordered whenever public investor creditors do not receive full and strict priority. The narrowing of this above-noted statutory discretion by judicial fiat has no proper place in these proceedings.

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[3] The District Court of Colorado in this case; *In re American Guaranty Corp.,* 221 F. Supp. 961 (D.R.I. 1963) appeal pending *sub nom. Securities and Exchange Commission* v. *Burton* (1st Cir. No. 6623); *In re Crumpton Builders, Inc.* (M.D. Fla. No. 63-4-2T) appeal pending *sub nom. Securities and Exchange Commission* v. *Crumpton Builders, Inc.* (5th Cir. No. 20712); and *In the Matter of Canandaigua Enterprises Corp.* (W.D.N.Y. 1964) appeal pending (2nd Cir. No. 29012)

A basic consideration in the case at bar is whether or not a plan of arrangement under Chapter XI is for the best interests of creditors where the former stockholders, some of whom had also made loans to the company in addition to their equity investment, receive an 18% stock interest in the reorganized company (12% from their equity interest including the rental system and 6% from loans on a scaled-down basis much more drastic than that applied to other creditors), this stock interest to be non-voting and without dividends for five years (R. 148). Such a plan can perfectly well be fair and equitable and definitely in the best interests of creditors if the alternative is liquidation in bankruptcy or under expensive Chapter X. See the next to last paragraph in the Circuit Court's Opinion in this case (325 F. 2d at 53, R. 161) and *In re Village Men's Shops, Inc.*, 186 F. Supp. 125 (S.D. Ind. 1960), which note that "in the best interests of creditors" means broadly that a Chapter XI plan is to be preferred if it yields more to the creditors than would a liquidation. See also *Bartle v. Markson Bros., Inc.*, 314 F. 2d 303 (2d Cir. 1963), in which, while reversing the confirmation of a plan on other grounds, the court (Clark, J.) stated:

> Since, however, the amount to be received under the plan of arrangement compares favorably with probable liquidation payments and since the creditors were fully informed in advance, we do not regard the referee's finding the arrangement was in the best interests of the creditors as necessarily erroneous in law. (314 F. 2d at 305)[4]

[4] The phrase "in the best interest of the creditors" is the same phrase in former Section 12d of the Bankruptcy Act before the revision of 1938 and it was interpreted:

> . . . to require a comparison between what creditors would receive under the composition offer and what they would receive in a liquidation of the estate. . . . Where creditors would not realize as much in liquidation as they would receive under the composition offer, or where it is uncertain that liquidation would result in any appreciable advantage over the composition offer, the composition under §12 was for the best interests of creditors. 9 Collier on Bankruptcy, (14th Ed.) §9.17, pp. 280-281.

Chapter X by the express words of Section 130(7) (11 U.S.C. §530(7)) applies only when by specific facts it is shown "why adequate relief cannot be obtained under Chapter XI." This and the provision of Section 328 that transfer depends upon a finding that "the proceedings should have been brought under Chapter X" show that Chapter XI is the normal avenue for relief of a distressed corporation with only unsecured debt.

This analysis is further confirmed by the provisions of Section 147 of Chapter X (11 U.S.C. §547) providing for the transfer to Chapter XI of a Chapter X proceeding on the grounds that "adequate relief can be obtained by the debtor under Chapter XI.".

The Petitioner's real complaint here is that the plan is not on Chapter X standards fair to the public investor creditors (the trailer owners). This is not the question here. The proper way to raise that issue is on a review of the order confirming the plan. The S.E.C. did intervene to do this as in *In re Lea Fabrics*, 272 F.2d 769 (3rd Cir. 1959). The appeal from such an order, not presented in this case, directly raises the question of whether the plan met the requirement that it was "for the best interests of creditors and is feasible." This type of procedure is well illustrated in *Bartle* v. *Markson Bros., Inc.*, 314 F.2d 303, *supra*, where the plan was disapproved on an appeal by creditors because there had been no proper explanation of missing assets.

The appeal (C.C.A. No. 7474; R. 152) from the confirmation decree, which is not covered by the certiorari writ as above noted, raises directly the issue of best interests of creditors of all kinds and brings all facts under review, whereas this appeal from a denial of the motion under Section 328 really does not involve the question of the

plans' compliance with the requirements for confirmation in Sec. 366(2) (11 U.S.C. §766(2)).

This becomes very clear when one realizes there is no Congressional intent shown to exclude this type of case from Chapter XI; that under Chapter XI debtors can be helped if the plan of arrangement is "in the best interests of creditors," an appealable determination; and that the cumbersome procedures of Chapter X involving much time and money afford no better basis for action by the S.E.C. than its intervention in a Chapter XI proceeding to determine whether the plan is "in the best interests of creditors," large and small, public and private.

In the case at bar, with all creditors on an unsecured basis, except about $10,000 of priority tax items and a chattel mortgage, there is nothing to indicate "adequate relief cannot be obtained" in a Chapter XI proceeding. If there is in fact something objectionable about the proposed reorganization, surely it is in the proposed plan of arrangement rather than in the use of Chapter XI as the avenue of reorganization.

On this analysis also the Petitioner's argument in Point B, pp. 39 to 49 of its brief is ineffective on the question presented and subject to review here under the granted writ.

This question of the propriety of the preservation of stockholder interests is quite independent of other issues of mismanagement, violation of the Securities Act of 1933 in the distribution of securities and other separate possible disciplinary action which the Commission might feel called upon to take. These other issues should not obscure or affect the decision on the only question which is covered by the certiorari writ in this case.

The cumbersome proceedings and S.E.C. report involved in a Chapter X proceeding are not necessary to protect creditors. Congress delegated that duty to the judge in Section 366 (2) (11 U.S.C. §766(2)) by providing that before confirmation he must find the plan "in the best interests of creditors," which, of course, includes the trailer-owner public investor in this case. This necessity for court approval is a statutory protection actually exercised in this case by the District Judge (R. 146), who required changes in the rate at which shares of the new corporation were issuable, so that management people who were creditors received far less for their claims than other creditors.

The Petitioner's principal reliance is upon the so-called rule of strict priority which would appear in this case to mean that none of the shares of the new company could under the plan be distributed to former shareholders. This strict priority principle emanates from *Northern Pacific Railway Co.* v. *Boyd,* 228 U.S. 482 (1913), but it "does not . . . require . . . [payment of] unsecured creditor[s] in cash as a condition of stockholders retaining an interest" (228 U.S. 508). The *Boyd* case did not involve any federal Act under which creditors' rights were affected by statute. It was a voluntary change by a controlling stockholder who caused a foreclosure which cut off a judgment creditor, Boyd.

The other case which stands at the root of the so-called strict priority rule is *Case* v. *Los Angeles Lumber Products Company, Ltd.,* 308 U.S. 106 (1939). There a confirmed plan under old Section 77B was reversed because shareholders of the debtor "insolvent both in the equity and bankruptcy sense, with no indicated equity received 23% of the vote in the reorganized company." The court held that the words "fair and equitable" in Section 77B re-

quired that absolute priority be given the claims of creditors, although the court acknowledged that this requirement did not have to be met by a cash payment (308 U.S. at 116, 117).

The principle of those cases no longer applies to a Chapter XI proceeding. Congress, by the 1952 Amendments to Section 366 of the Bankruptcy Act (11 U.S.C. §766), deleted the former requirement of "fair and equitable", so that the plan need now be only "for the best interests of creditors" and "feasible." Had there been any intention on Congress's part to provide that, under a plan, stockholders may not receive anything until the creditors are paid in full, the 1952 Amendments would certainly have not inserted the last clause of Section 366 which specifically provides that retention of a stockholder's interests is proper under a Chapter XI plan.

The Commission argues to the contrary that the 1952 deletion of the words "fair and equitable" was merely a "qualifying" and "uncontroversial" amendment intended to do no more than allow the scaling down of trade creditors' claims without any change in the claims of junior securities holders. It is difficult to understand how the Commission may argue at one point that "fair and equitable" are words of art importing the definite and fixed requirement of absolute priority and at another point that the deletion of this phrase from the statute is not intended to affect the substantive requirements the words have been construed to import.[5]

[5] These Amendments were far from "uncontroversial" as indicated by the examples in 9 Collier on Bankruptcy (14th Ed.) §9.18(2.1) pp. 304-305; and H. R. Rep. No. 2320, 82nd Cong., 2nd Sess., p. 21 (1952); 1952 U.S. Code Cong. & Admin. News pp. 1981-82 (objection of Treasury Department).

<u>There is absolutely nothing in Chapter XI or the 1952 Amendments which suggests, as the Petitioner argues, the use of the chapter is limited to arrangements with trade creditors.</u>

The legislative history of the 1952 Amendments indicates very clearly that their purpose was to do away with notions of absolute priority in Chapter XI proceedings. In H. R. Rep. No. 2320 (the Committee Report on the basis of which the 1952 Amendments were enacted), 82nd Cong., 2d Sess., p. 21 (1952), it was stated:

> In fact, however, the fair and equitable rule as interpreted in *Northern Pacific Railway* v. *Boyd,* 228 U.S. 482; (*supra*) and *Case* v. *Los Angeles Lumber Products Co., Ltd.,* 308 U.S. 106, (*supra*) cannot realistically be applied in a Chapter XI, XII or XIII proceeding.
>
> . . .
>
> The proposed amendment is designed to remove the fair and equitable provision, and by the paragraph added to each of the amended sections it is made clear that the rule of the *Boyd* and *Los Angeles* cases shall not be operative under those three chapters. U.S. Code Cong. & Admin. News, 1952, pp. 1981, 1982

These Amendments can have no other significance than that Congress intended Chapter XI to be available to all types of corporations with only unsecured debt which are in trouble, excluding only those where it should be shown that adequate relief could not be obtained under Chapter XI. Had there been any intention to exclude corporations with public investor creditors or those where stockholders were left with some interests under the plan, it would have been very easy for Congress to say so. These Amendments make clear that the judicial rule of strict priority enunciated years ago under the peculiar circumstances of the

Boyd case, *supra*, has no bearing on plans of arrangement which were "feasible." Though "strict priority," i.e., payment in full before junior claims get anything, may sometimes be a factor in making a plan "feasible," it is not today a requirement for confirmation of a Chapter XI plan.

The purpose of this review is to have this Court engraft upon the statute an exception in cases where some of the creditors are public investors. As authority for this proposition of absolute priority for public investors, the Commission points to language in the case of *General Stores Corp.* v. *Shlensky, supra*, where the Court gave the following as one of several examples of when Chapter X was more suitable than Chapter XI:

> Readjustment of all or a part of the debt of an insolvent company without sacrifice by the stockholders may violate the fundamental principle of a fair and equitable plan. (Citing two cases decided before the amendments to Section 366) (350 U.S. at 466)

It is the Commission's contention that this language represents a holding by the Supreme Court that there still must be absolute priority for the claims of public investor creditors in any plan of arrangement, despite the Amendments to Section 366. If this is true, then absolute priority is still the rule as to claims of all creditors (including trade creditors), since the language used by the court makes no distinction in the kind of creditors entitled to a "fair and equitable" plan. The result of this would be that the amendments to Section 366 were absolutely meaningless.

The Commission's argument that creditors must still receive absolute priority despite the amendments to Section 366 relies almost solely on this broad hypothetical illustration without delving into the factual or stylistic context of

the case in which it was given. In the first place, notwithstanding the Commission's contention to the contrary, the Supreme Court has never given full consideration to the 1952 Amendments to Section 366.[6] Secondly, a careful reading of the quotation will show that it is inappropriate in a case where the stockholders, by the terms of a plan of arrangement, also make sacrifices in order to aid in the rehabilitation of the debtor. Thus, in the case at bar the stockholders are giving up their complete ownership of the debtor to become minority shareholders in the new corporation without vote or dividends for five years. Also, management shareholders who have unsecured debts owed by the corporation are receiving for those debts about half of what other unsecured creditors receive. Further sacrifices by management shareholders include a five-year suspension on voting rights, dividend rights, and rights in liquidation (R. 148).

Also, it should be noted that the language in the quotation is permissive—readjustment without sacrifice by stockholders "may violate the fundamental principle of a fair and equitable plan." Finally, the court merely states that in such a hypothetical circumstance, "Chapter X affords a more adequate remedy than Chapter XI," which is not the same thing as saying that Chapter XI is inadequate or that it is an abuse of discretion of the District Judge to refuse a transfer to Chapter X. In this context it must be remembered that the Court in *General Stores* was reviewing the decision of lower courts granting a motion to transfer

[6] "Since the *Realty* decision to no small degree turned on the enforcement of the 'fair and equitable' rule, it is noteworthy that no consideration was given by the lower courts, and none is given by this court, to the significance of this amendment by Congress." Frankfurter, J., dissenting in *General Stores Corp.* v. *Shlensky*, *supra,* 350 U.S. at 472 (1956)

proceedings to Chapter X rather than the denial of such a motion.

It is therefore respectfully urged that the decision of the Circuit Court be affirmed.

II. The Decision in this Case Should go no Further Than to Deal With the Particular Facts Presented, Because in the Burton Case Now Before the Court of Appeals for the First Circuit, the Only Sacrifice by Public Investor Creditors is at Most a Two-Year Waiver of Interest on Their Claims and Because the Plan in That Case Provides Safeguards Similar to Those Found in Chapter X, Making That Case Far Different in Spirit and in Law From the Case at Bar.

The above considerations are particularly applicable to the First Circuit case in which those submitting this brief are parties. In that case a Receiver is in possession of the debtor, and the plan of arrangement envisages his control in distributing funds during the time until all creditors are paid in full, except for a waiver of interest pending judicial proceedings not in excess of two years.

In the *Burton* case the stockholders have no voice in the operation of the business or its further development without creditor assent until all creditors are paid, except for a limited veto subject to arbitration on sales of assets in excess of $20,000. It would be most unfair to force the debtor in that case, American Guaranty Corporation, into Chapter X simply because of the waiver of interest negotiated for the benefit of public investors holding subordinated debt and stocks.

The two-year time limit on this waiver, which was necessary only because of the delays inherent in court pro-

cedures, is not a serious flaw in a plan even on a strict priority basis, because it is only reasonable that the interest cost resulting from such inevitable court delays in processing this type of situation should not be borne entirely by the stockholders and junior creditors (many of whom are small public investors). Other substantial expenses of negotiation, administration and litigation do come from funds that would otherwise be available for publicly held subordinated debt and stocks. That is enough burden for these interests to bear, and it is eminently fair that the interest waiver put a part of the arrangement expense upon the senior creditors. In short, the plan in the *Burton* case is both "fair and equitable" and not contrary to any rule of strict priority. However, it is urged that the plan is not required to conform to any such rule.

Reliance by the Petitioner on certain provisions of Chapter X, notably those with regard to an independent trustee's developing the plan of reorganization and an S.E.C. investigation and report as provided for in Sections 156, 158, 167, 174 and 175 of Chapter X (11 U.S.C. §§556, 558, 567, 574 and 575) are not criteria for a holding that a District Judge abused his discretion under Section 328 (11 U.S.C. §728) because in the *Burton* case: (1) an independent receiver is in possession with qualified counsel and power to enforce the corporation's claims for mismanagement; (2) under the direction of the referee an investigation of possible misdeeds in line with the provisions of Section 21(a) of the Bankruptcy Act (11 U.S.C. §44(a)) is now current; (3) the Petitioner, as an intervenor, can participate in the necessary determination by the referee and the court just as effectively as in a Chapter X proceeding; (4) the independent receiver charged with the duty of collecting assets can prosecute just as effectively as an inde-

pendent trustee causes of action belonging to the estate; and (5) the plan of arrangement was prepared and developed in large measure by the creditors, not the debtor.

In connection with (2) above, see *Grayson-Robinson Stores, Inc.* v. *Securities and Exchange Commission, supra,* 320 F. 2d 940 (2d Cir. 1963), in which Judge Friendly stated that if there is a Section 21(a) investigation and the S.E.C. does not particularize in what respects this investigation is not complete, then, although a Section 21(a) investigation may not be as thorough as one by a trustee under Chapter X, it can be said that the District Judge:

> . . . properly looked at what had already been done and what may be done in the future in determining whether the benefits of a Chapter X investigation would outweigh the detriments of transfer to that chapter. (320 F. 2d 949)

The appendix to this brief shows that the Chapter X protective provisions relied on by the Petitioner in arguing transfer to that Chapter have been incorporated into the modified plan of arrangement in the *Burton* case, so that the comparative summary of Chapter X and Chapter XI processes in the Appendix to Petitioner's brief cannot show in the *Burton* case any inadequacy of the plan because of an alleged lack of protective provisions.

The Commission is attempting to engraft an absolute priority requirement on all Chapter XI proceedings involving public investor creditors by means of the following syllogism:

1. The *Boyd* and *Los Angeles* cases say all corporate rehabilitations must give absolute priority to the claims of creditors.

2. Congress deleted from Chapter XI the "fair and equitable" provision upon which was based the absolute priority requirement.

3. Therefore, Chapter XI cannot be used if it violates the rule of *Boyd* and *Los Angeles* (at least when the creditors are public investors).

Patently, the above construction does not hold water. No. 3 should read: "Therefore, the rule of *Boyd* and *Los Angeles* no longer applies to Chapter XI arrangements."

To a certain extent the Commission has succeeded in its efforts. It has been noted in *Collier on Bankruptcy:*

> There is, however, some indication that the 'fair and equitable' test may be reintroduced in Chapter XI by indirection. Suggestive of this are several cases which, in ruling that the proceeding involved should have been brought under Chapter X rather than Chapter XI, gave as a reason not only that there was need of independent and thorough analysis by a court or trustee but also that a scaling down of the claims of creditors without some compensating advantage to them which is ~~prior~~ to the rights of stockholders would prevent a fair and equitable arrangement from being consummated under Chapter XI. 9 Collier on Bankruptcy (14th Ed.) Para 9.18(2.1) at 306

The author concludes, however:

> Since the legislative elimination of the 'fair and equitable' test, use and reliance on these words in view of the past interpretation, should not be continued. While several decisions have continued to refer to the 'fair and equitable' test, other and sound reasons for favoring Chapter X of Chapter XI were present in those cases. *Ibid.*

Statement of Committee of Creditors.

The official Committee of Creditors of America Guaranty Corporation, the Debtor involved in the case of *Securities*

and Exchange Commission v. *Burton,* now pending before the Court of Appeals for the First Circuit (Docket Number 6223) concurs in the position argued in this *amicus curiae* brief. It believes that the needs-to-be-served criteria developed under this Court's decision in *General Stores Corp.* v. *Shlensky,* 350 U. S. 462 (1956), have provided the United States District Courts with the requisite flexibility to prescribe remedies for the extraordinary variety of economic ills which can and do beset corporate debtors. The rigid position now urged by the Petitioner is not a satisfactory or practical alternative for a discriminating determination of appropriate relief in each particular case. See Weintraub & Levin, "Reorganization or Arrangement: An Analysis of Contemporary Trends in Recent Cases," 1963 *Journal Nat'l. Ass'n. Referee in Bankruptcy* 103.

III. Conclusion.

For the reasons stated above, the Court should not rule that Congress intended in a Chapter XI arrangement that absolute priority must be given the claims of public investor creditors, so that, if the arrangement attempts so to deny absolute priority, *ipso facto* the proceeding should be dismissed or transferred to Chapter X. Rather the Court should examine the bankrupt corporation and the claims of its creditors to determine whether Chapter XI meets the "needs to be served."

Four judges have so determined and confirmed the plan as "in the best interests of creditors and feasible", and the confirmation is not under review here. Certainly on the basic question at bar it is clear that the District Judge was not too wide of the mark, or guided by such faulty standards, that his judgment in refusing a transfer to Chapter X was an abuse of discretion.

It is our position and hope that in its decision in this case the Court lay to rest the Securities and Exchange Commission's illogical position: that the elimination of "fair and equitable" from Chapter XI makes that Chapter unsuitable whenever an arrangement under it denies in any way absolute priority to the claims of public investor creditors.

Consequently, we urge that the decision in this case should not touch a Chapter XI proceeding such as is presented in the *Burton* case.

Respectfully submitted,

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September 18, 1964

Appendix.

The Petitioner contends that public-investor creditors can only be adequately protected by proceeding under Chapter X. As the following table shows, this is not necessarily so. In the plan of arrangement under Chapter XI of American Guaranty Corporation involved in *Securities and Exchange Commission v. Burton* (1st Cir. No. 6623) provisions substantially identical to the protections afforded by Chapter X have been included.

Item from Petitioner's Comparison and Description	*Substantially Identical Provision in American Guaranty Corp. Plan of Arrangement*
1-3. Independent Trustee.	Independent Receiver in possession.
4-6. Examination and reports on Debtor's Finances and Conduct.	Referee's designee Charles J. McGovern, Esq., of the Providence Bar to investigate in line with Section 21(a) of the Bankruptcy Act (11 U.S.C. §44(a)) and report to S.E.C., creditors and stockholders (Art. V C).
7-8. Formulation and filing of Plan by Trustee.	Plan developed after careful negotiations with help of the Referee between Debtor, creditors and stockholders, each represented by independent counsel.
9. Assistance of S.E.C.	S.E.C. is a party, having been permitted to intervene.

10-12.	Nature of Plan and Submission.	Plan developed with assistance of Referee, transmitted to creditors subject to finding of "best interests of creditors."
13-14.	Acceptances.	Much more than two-thirds of creditors have approved and stock rights suspended but not permanently affected (Art. II C).
15.	Classes affected.	Only unsecured debts involved.
16.	Participation in proceeding.	Many have entered appearances and have been heard.
17.	Control of representatives.	Creditor executive committee to have Referee approval.
18-23.	Elements concerning: Indenture Trustees, Lists of Security Holders, Compensation and allowances, Subsidiary Corporations, Future Management, and the charter of the Reorganized Company.	These elements are either not of a "protective nature," or they are available, or there is provision for Referee or Court approval.

Consents to Filing of Amicus Curiae Brief.

Dear Mr. Jenckes:

As requested in your letter of August 5, 1964, I am happy to consent to the filing in the above case of a brief *amicus curiae* on behalf of the State Mutual Life Assurance Company of America, The George Putnam Fund of Boston and the Putnam Management Company, Inc. As discussed in our previous correspondence, my consent also extends to the joining in such brief of the Creditors' Committee that is a party in the pending case of *Securities and Exchange Commission* v. *Burton,* C.A. 1, No. 6223.

There is inclosed an extra copy of this letter, so that you can file the original with your brief, as required by Rule 42(2) of the Revised Rules of the Supreme Court.

Sincerely,
/s/ Archibald Cox

Archibald Cox
Solicitor General

American Trailer Rentals Company, the above-named respondent, consents to the filing of a brief of an *amicus curiae* on the merits in the above entitled matter by Marcien Jenckes, Esquire, of Choate, Hall & Stewart, Boston, Massachusetts. This consent is given pursuant to Rule 42(2).

AMERICAN TRAILER RENTALS COMPANY
By /s/ Arthur W. Burke, Jr.

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American Trailer Rentals Company